

Company Note

Beijing Enterprises Urban Resources Rating **OUTPERFORM**

1H21 earnings in line with our estimate, mgmt. remained positive on project bidding target

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Anson Tang
(852) 2683 3225
anson.tang@icbci.icbc.com.cn

Nelson Lee, CFA, FRM
(852) 2206 8357
nelson.lee@icbci.icbc.com.cn

Sector **Renewables & Environmental**

Key Data	
Ticker	3718.HK
Price (27 Aug)	HKD 0.80
Target price	HKD 1.14
Upside	42%

52W High	HKD 2.54
52W Low	HKD 0.76
Mkt. Cap. (HKD mn)	2,880
Mkt. Cap. (USD mn)	372
Total Issued Shares (mn)	3,600
Avg. 3mths t/o (HKD mn)	5

Shareholdings Structure	
Beijing Enterprises Water Group	28.0%
Mr. Tang Wai Meng	7.0%
T. Rowe Price Associates	5.9%
Company Directors	7.4%
Free float	51.6%

Price performance



%	1m	3m	6m
3718.HK	1.3	(32.8)	(37.0)
HSI	1.3	(12.7)	(12.3)

Source: HKEx, Bloomberg, Company data, ICBCI estimates.

BEUR's earnings grew 14% YoY to HKD 249mn in 1H21, which was in line with our estimate of HKD 250mn. However, excluding subsidy amount (increase in VAT relief and reduction of social welfare and security contributions in 1H20) due to COVID-19 outbreak, BEUR would have recorded 43% YoY growth in 1H21. The earnings growth was mainly due to increase in hazardous waste treatment revenue, environmental hygiene service revenue and waste electrical and electronic equipment treatment income, which was partly offset by the decrease in blended gross margin on the back of the decline in VAT relief and reduction of social welfare and security contributions, and the reduction in hazardous waste disposal fee. BEUR signed 2 environmental hygiene services projects with annual service fee of RMB 16mn, which only accounts for 2% of its 2021 bidding target of RMB 0.84bn. Mgmt. emphasized that they are not going to revise the project bidding target. We conservatively revised our sanitation service projects bidding assumption to RMB 0.5bn for 2021E. In addition, hazardous waste disposal and recycling & reuse operating capacity reached to 351kt/yr and remained at 250kt/yr respectively as of end-1H21 and 3 hazardous waste disposal projects under construction are likely to enter into operation in 2H21E. We revised our 2021E-2023E net profit forecasts by -20% to 4% to reflect our assumption of lower annual service fee of environmental hygiene projects bidding and lower utilization rate of hazardous waste treatment facilities. Current valuation of BEUR looks undemanding at 6x 2021E P/E. Maintain OUTPERFORM rating with TP adjusted to HKD 1.14 with the revised earnings, which is based on our SOTP valuation with 9x 2021E P/E for its environmental hygiene services segment and 7x 2021E P/E for other environmental segments. Our TP is equivalent to 2021E P/E of 8x, with potential upside of 42%.

1H21 earnings +14% YoY, in line with our estimate. BEUR's 1H21 earnings grew 14% YoY to HKD 249mn, which was in line with our estimate of HKD 250mn. Excluding subsidy effect (increase in VAT relief and reduction of social welfare and security contributions in 1H20) due to COVID-19 outbreak, BEUR would have recorded 43% YoY growth to HKD 223mn in 1H21. BEUR's earnings growth was mainly due to: 1) 29% YoY growth in environmental hygiene service revenue on the back of higher effective annual service fee; 2) 95% YoY increase in revenue of hazardous waste disposal on the back of 172% YoY increase in treatment volume, while partly offset by 28% YoY decrease in treatment fee; 3) 49% YoY increase in revenue of hazardous waste reuse & recycling on the back of 5% YoY increase in treatment volume and 43% YoY increase in treatment fee; and 4) 54% YoY increase in waste electrical and electronic equipment treatment income. It is worth noting that blended gross margin (GPM) declined 4ppts to 29% in 1H21 mainly due to the decrease in VAT relief and reduction of social welfare and security contributions. In particular, GPM in environmental hygiene segment dropped 4ppts YoY to 27% in 1H21, which was partly offset by 0.3ppt increase in hazardous waste treatment GPM on the back of normal facilities operation after outbreak period (1H21: 40.1% vs. 1H20: 39.9%).

Mgmt. still remained positive view on the project bidding target. BEUR won 2 environmental hygiene services projects with annual service fee of RMB 16mn and total contract value of RMB 16mn in 1H21, which only accounts for 2% of its projects bidding target of annual service fee reaching RMB 0.84bn. However, mgmt. mentioned that the target will not be changed and they are confident on achieving its project bidding target. According to our channel check, BEUR was not active in the

project bidding process as they were not in the list of the govt. project bidding documents. Therefore, we revised our 2021 annual service fee assumption from RMB 0.72bn to RMB 0.5bn. We expect BEUR's total annual service fee will increase to RMB 3.5bn in 2021E, and further increase to RMB 4.1bn in 2023E.

Hazardous waste treatment segment expected to grow in the coming years. The hazardous waste disposal operating capacity reached 351kt/yr as of end-1H21 vs. 339kt/yr as of end-20, while the recycling & reuse operating capacity remained at 250k/yr as of end-1H21. There were 3 hazardous waste disposal projects with capacity of 85kt/yr under construction in 1H21, and we expect these projects to be commissioned in 2021E. Mgmt. mentioned that the treatment fee of hazardous waste disposal segment is likely to have reached the bottom level and we expect to see recovery in 2H21E. We estimate the proportion of hazardous waste treatment segment in the revenue mix will increase from 14% in 2020 to 21% in 2023E on the back of 24% and 5% CAGR of hazardous waste disposal and recycling & reuse effective capacity growth.

2021E-2023E net profit revised by -20% to 4%. Earnings revision was to reflect: (1) our assumption of lower annual service fee of environmental hygiene projects bidding; (2) lower hazardous waste disposal fee; (3) lower utilization rate of hazardous waste treatment facilities; (4) lower gross margin of hazardous waste disposal segment; (5) higher administrative expense; and (6) higher effective tax rate, which partly offset by: (1) higher hazardous waste reuse & recycling fee; (2) higher waste electrical and electronic equipment treatment; (3) high gross margin of hazardous waste reuse & recycling segment and (4) lower average cost of debt.

Maintain OUTPERFORM, current valuation undemanding at 6x 2021E P/E. We maintain OUTPERFORM rating with TP adjusted to HKD 1.14 with the revised earnings, which is based on our SOTP valuation with 9x 2021E P/E for its environmental hygiene services segment and 7x 2021E P/E for other environmental segments. Our TP is equivalent to 2021E P/E of 8x, with potential upside of 42%.

Valuation Statistics

YE	Turnover	Net profit	EPS	EPS	PER	EV/	PBR	ROE	Net debt/
31 Dec	HKD mn	HKD mn	HK cents	chg %	x	EBITDA	x	%	equity
						x	x		%
2019	2,711	281	10.4	-34.6%	7.7	3.1	1.2	16.7	15.0
2020	3,520	427	12.0	14.9%	6.7	2.1	1.0	17.7	0.9
2021E	4,323	492	13.7	14.3%	5.8	1.8	0.8	15.1	8.8
2022E	4,797	533	14.8	8.3%	5.4	1.6	0.7	14.1	13.7
2023E	4,906	575	16.0	7.9%	5.0	1.4	0.6	13.3	20.3

Source: Company, ICBCI estimates

Exhibit 1: 1H21 results snapshot

FY-end Dec (HKD m)	1H20	1H21	YoY change (% or ppt)	Our comments
Revenue	1,546	2,111	37%	
- Environmental hygiene services	1,266	1,637	29%	<ul style="list-style-type: none"> • 2 projects newly added in 1H21 • Total contracted area remained at 194mn sq.m., with average revenue of HKD 6.4 per sq.m. in 1H21 (1H20: HKD 6.2 per sq.m.) • Secured projects with RMB 16mn and RMB 16mn in terms of annual service fee and total contract value respectively in 1H21
- Hazardous waste treatment business	193	341	76%	<ul style="list-style-type: none"> • Hazardous waste disposal operating capacity reached to 351kt/yr in 1H21 • Hazardous waste recycling and reuse operating capacity remained at 250kt/yr in 1H21 • Disposal volume 172% YoY to 107kt, with average treatment fee -28% YoY to HKD 2,077/ton • Recycling and reuse volume +5% YoY to 30kt, with average treatment fee +43% YoY to HKD 4,014/ton on the back of the increase in the market price of methanol • 3 Hazardous treatment projects under construction and 3 hazardous treatment projects under planning stage in 1H21
- Waste electrical and electronic equipment treatment business	87	133	54%	
Direct costs and operating expenses	-1,038	-1,492	44%	
Gross profit	508	619	22%	
Gross profit margin	33%	29%	-3.5ppts	<ul style="list-style-type: none"> • Gross margin in environmental hygiene services segment decreased 4ppts YoY to 27.4% due to the decrease in relief related to VAT and reduction of social welfare and security contributions in 1H21 • Gross margin in hazardous waste treatment business rose 0.3ppt YoY to 40.1% due to normal operation after COVID-19 outbreak and the increase in the market price of methanol, while partly offset by the effect of the waste disposal fee reduction • Gross margin in waste electrical and electronic equipment treatment business reduced 7ppts YoY to 25% in 1H21
SG&A expense	-144	-211	46%	<ul style="list-style-type: none"> • Admin to sales ratio was 10% in 1H21 (1H20: 9.3%) • Staff cost +45% YoY in 1H21
Other gain/loss	23	35	49%	<ul style="list-style-type: none"> • Govt. grants +1% YoY in 1H21 • VAT refund -9% YoY in 1H21
Operating profit	387	442	14%	
Operating margin	25%	21%	-4.1ppts	
Finance expenses	-36	-38	6%	
Share of profit/(loss) of a joint venture	2	3	42%	• Net gearing was 10% as of end-Jun21, vs. 1% as of end-Dec20
Profit before taxation	353	407	15%	
Income tax expenses	(82)	(101)	23%	
Effective tax rate	23%	25%	1.5ppts	
Net profit/(loss) attributable to shareholders	218	249	14%	• 1H21 net profit in line with our estimates, i.e. HKD 250mn
Net profit margin	14%	12%	-2.3ppts	
EPS (HKD cent) - basic and diluted	6.2	6.9	12%	

Source: Company, ICBCI estimates

Exhibit 2: Earnings revision

	2021E			2022E			2023E		
	Old	New	%	Old	New	%	Old	New	%
Revenue (HK\$ mn)	4,382	4,323	-1.3%	5,228	4,797	-8.2%	5,914	4,906	-17.0%
Gross profit (HK\$ mn)	1,241	1,271	2.5%	1,513	1,364	-9.9%	1,760	1,450	-17.6%
Operating profit (HK\$ mn)	889	898	1.0%	1,127	965	-14.3%	1,330	1,043	-21.6%
Pre-tax profit (HK\$ mn)	800	821	2.6%	1,027	889	-13.5%	1,213	959	-20.9%
Net profit (HK\$ mn)	483	492	1.9%	621	533	-14.1%	733	575	-21.5%
EPS (HK cents)	13.4	13.7	1.9%	17.2	14.8	-14.1%	20.4	16.0	-21.5%
	Old	New	ppt	Old	New	ppt	Old	New	ppt
Gross margin	28%	29%	1.1	29%	28%	-0.5	30%	30%	-0.2
Operating margin	20%	21%	0.5	22%	20%	-1.4	22%	21%	-1.2
Net profit margin	11%	11%	0.4	12%	11%	-0.8	12%	12%	-0.7
ROE	15%	15%	0.3	16%	14%	-2.2	16%	13%	-3.0
ROA	8%	8%	0.2	9%	8%	-0.9	9%	8%	-1.2

Source: Company, ICBCI estimates

Exhibit 3: Income statement

HKD mn	2019	2020	2021E	2022E	2023E
Revenues	2,711	3,520	4,323	4,797	4,906
Cost of Sales	(1,928)	(2,433)	(3,052)	(3,433)	(3,455)
Gross Profit	783	1,087	1,271	1,364	1,450
Other revenue	60	70	86	96	98
SG&A expenses	(338)	(382)	(460)	(494)	(505)
Profit from operations	506	775	898	965	1,043
Finance costs	(72)	(72)	(77)	(77)	(84)
Share of loss of a joint venture and associate	0	1	0	0	0
PBT	433	704	821	889	959
Income tax	(87)	(163)	(205)	(222)	(240)
Profit for the year	346	540	616	667	719
Discontinued operation	6	0	0	0	0
Profit attributable to Equity shareholders of the Company	281	427	492	533	575
Non-controlling interests	71	114	123	133	144
Basic EPS (HK cents)	10.4	12.0	13.7	14.8	16.0

Sources: Company data, ICBCI estimates

Exhibit 4: Balance sheet

HKD mn	2019	2020	2021E	2022E	2023E
Current assets	2,287	3,539	3,382	3,366	3,301
Inventories	45	47	65	72	74
Trade and bills receivables	775	1,112	1,166	1,295	1,325
Prepayments, deposits and other receivables	85	106	202	225	230
Cash and cash equivalents	1,052	1,725	1,307	1,041	855
Other current assets	330	548	643	733	818
Non-current assets	2,700	3,579	4,497	5,386	6,493
Property, plant and equipment	2,083	2,679	3,495	4,400	5,536
Trade receivables	25	122	148	155	156
Prepayments, deposits and other receivables	115	70	202	225	230
Other non-current assets	477	709	652	607	571
Total assets	4,987	7,118	7,879	8,752	9,794
Current liabilities	1,618	2,322	2,154	2,316	2,464
Bank and other loans	564	986	673	688	802
Trade and other payables	161	233	237	263	269
Other current liabilities	893	1,103	1,244	1,365	1,393
Non-current liabilities	1,112	1,129	1,443	1,486	1,662
Bank and other loans	826	773	1,010	1,032	1,203
Others	286	357	433	454	459
Total Liabilities	2,730	3,451	3,596	3,802	4,126
Equity	2,258	3,667	4,283	4,949	5,669
Share capital	270	360	360	360	360
Retained earnings	1,544	2,652	3,144	3,677	4,253
Non controlling interest	444	656	779	912	1,056
Total equity and liabilities	4,987	7,118	7,879	8,752	9,794

Sources: Company data, ICBCI estimates

Exhibit 5: Cash flow statement

HKD mn	2019	2020	2021E	2022E	2023E
Operating cashflow	636	673	855	1,076	1,276
Profit before tax	440	704	821	889	959
Deprec & Amort.	237	317	383	467	588
Finance costs	72	72	77	77	84
Working capital chg	(11)	(280)	(199)	(110)	(90)
Others	(102)	(139)	(227)	(246)	(264)
CF from IA	(258)	(1,014)	(1,121)	(1,302)	(1,664)
Purchase of PPE	(882)	(977)	(1,142)	(1,326)	(1,688)
Other investments	623	(37)	22	24	25
CF from FA	7	904	(153)	(39)	201
Net borrowings	117	303	(76)	37	285
Share issuance	0	603	0	0	0
Dividends	0	(4)	0	0	0
Interest paid	(64)	(63)	(77)	(77)	(84)
Others	(46)	64	0	0	0
Net cash flow	384	563	(418)	(266)	(186)

Sources: Company data, ICBCI estimates

Exhibit 6: Financial ratios

	2019	2020	2021E	2022E	2023E
YoY growth rate					
Revenue	46%	30%	23%	11%	2%
Gross profit	41%	39%	17%	7%	6%
Net profit	-35%	52%	15%	8%	8%
Profitability					
Gross margin	29%	31%	29%	28%	30%
Operating margin	19%	22%	21%	20%	21%
NP margin	10%	12%	11%	11%	12%
ROE	17%	18%	15%	14%	13%
ROA	7%	9%	8%	8%	8%
ROIC	11%	13%	12%	11%	11%
Liquidity					
Liabilities to Asset	55%	48%	46%	43%	42%
Net gearing ratio	15%	1%	9%	14%	20%
Liquid ratio	1.4	1.5	1.6	1.5	1.3
Quick ratio	1.4	1.5	1.5	1.4	1.3
Operating efficiency					
Asset turnover	0.5	0.6	0.6	0.6	0.5
Inventory turnover days	12	7	7	7	8
AR turnover days	98	100	99	97	101
AP turnover days	27	30	28	27	28
Per share ratios (HKD cents)					
EPS	10.4	12.0	13.7	14.8	16.0
BVPS	67	84	97	112	128
Valuation ratios					
P/E	7.7	6.7	5.8	5.4	5.0
P/B	1.2	1.0	0.8	0.7	0.6
EV/EBITDA	3.1	2.1	1.8	1.6	1.4

Sources: Company data, ICBCI estimates

Sales

Telephone: (852) 2683 3888

Fax: (852) 2683 3881

Research

Telephone: (852) 2683 3888

Fax: (852) 2683 3222

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ICBC International Research Limited

Address: 37/F., ICBC Tower, 3 Garden Road, Central, Hong Kong Tel: (852) 2683 3888 Fax: (852) 2683 3900

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